

INFORMATION BULLETIN

2006-5

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Measures Favouring Innovation

The purpose of this information bulletin is to describe the improvement to tax assistance provided for innovation granted to Québec companies under the refundable tax credit for scientific research and experimental development and the refundable tax credit for design.

For information on the issues dealt with in this information bulletin, contact the Secteur du droit fiscal et de la fiscalité at 418 691-2236.

The French and English versions of this bulletin are available at the ministère des Finances website at: www.finances.gouv.qc.ca

Paper copies are also available, on request, from the Direction des communications, at 418 528-9323.

Improved tax assistance to support R&D activities

Québec's system of tax assistance for scientific research and experimental development (R&D) is designed to encourage taxpayers who carry on a business in Québec and have an establishment there to carry out or increase R&D work relating to the carrying on of such business in Québec, consistent with the government's objective of increasing R&D expenditures to 3% of GDP by 2010.

In this regard, the R&D tax assistance measures were updated in the March 23, 2006 Budget Speech to reflect the new reality of the 21st century, more specifically in the context of the government economic development strategy released in 2005.¹ Briefly, the purpose of these changes is to allow greater participation by institutions in projects giving rise to tax assistance, and to encourage the emergence of partnerships in carrying out R&D activities in Québec.

These changes were consistent with the context of government support for the efforts made by Québec companies in the field of research and innovation.

The government's target regarding R&D depends largely on greater participation by companies in funding R&D expenditures.

In this context, and combined with the changes announced earlier, tax assistance for R&D will be improved.

Briefly, Québec's system of tax assistance for R&D currently includes four refundable tax credits. The most important of these four tax credits is the tax credit for R&D salaries. This tax credit alone accounts for 95% of the government's annual tax expenditure on account of refundable tax credits for R&D.²

The refundable tax credit for R&D salaries applies to the salaries a person pays to his employees where he himself carries out his R&D work in Québec and, where it makes use of a subcontractor with whom he is at arm's length, in particular, it applies to half the amount of the research contract.

The basic rate of the refundable tax credit is 17.5% but it can be increased up to 37.5% in the case of a Canadian-controlled corporation.

More specifically, the rate of this tax credit is 37.5% for a taxation year, in the case of a Canadian-controlled corporation whose assets, including the assets of associated corporations calculated on a world basis, do not exceed \$25 million for the preceding taxation year, reducing linearly to 17.5% where assets vary between \$25 million and \$50 million. The increased rate applies only to the first \$2 million of R&D expenditures.

¹ MINISTÈRE DU DÉVELOPPEMENT ÉCONOMIQUE, DE L'INNOVATION ET DE L'EXPORTATION, *The Québec Advantage – The Québec Government's Economic Development Strategy*, 2005.

² GOUVERNEMENT DU QUÉBEC, *Tax Expenditures – 2006 Edition*, October 2006, Part I.

To increase tax assistance to Québec companies that are active in R&D, but also to support the additional effort required of these companies to achieve the R&D expenditure funding target, the tax legislation will be amended to raise the thresholds of \$25 million and \$50 million above to \$50 million and \$75 million respectively.

The following table illustrates the effect of this increase in the thresholds in the case of assets ranging between \$25 million and \$75 million.

IMPROVED TAX ASSISTANCE TO SUPPORT R&D ACTIVITIES

Illustration of the increase in thresholds

Assets of the corporation (millions of dollars)	Existing rates (per cent)	New rates (per cent)
(25 or less)	37.5	37.5
30	33.5	37.5
35	29.5	37.5
40	25.5	37.5
45	21.5	37.5
50	17.5	37.5
55	17.5	33.5
60	17.5	29.5
65	17.5	25.5
70	17.5	21.5
75	17.5	17.5

This change will apply to R&D expenditures incurred after the day of publication of this information bulletin, regarding R&D work done after that day.

Improved tax assistance to support design activities

The refundable tax credit for design has two components and applies regarding certain expenditures that an eligible corporation incurs in relation to eligible design activities.

The first component concerns fashion design (design and pattern-drawing) and industrial design activities carried out in the course of an external consultation contract. The second component applies to salary expenditures incurred by a corporation regarding designers and pattern-makers it employs in the fashion sector, and designers it employs in the industrial sector.

The basic rate of the tax credit is 15% for these two components but, like the refundable tax credit for R&D salaries, it can be increased up to 30% in the case of a corporation whose assets, including the assets of associated corporations calculated on a world basis, varies between \$25 million and \$50 million for the preceding taxation year.

Since design activities are also important in the innovation process of Québec companies, the tax assistance in this regard will be improved in a manner similar to the improvement made to the refundable tax credit for R&D salaries.

Accordingly, the tax legislation will be amended to raise the thresholds of \$25 million and \$50 million mentioned above to \$50 million and \$75 million respectively.

This change will apply to eligible design expenditures incurred after the day of publication of this information bulletin, regarding eligible design activities done after that day.

